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Applied Research about the Pittsburgh Region's Nonprofit Sector

WHY ENGAGE?
Understanding the Incentive to Build Nonprofit Capacity

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ABOUT CAPACITY-BUILDING: GRANTMAKERS FOR EFFECTIVE ORGANIZATIONS (GEO) DEFINES ORGANIZATIONAL EFFECTIVENESS AS AN ORGANIZATION'S ABILITY TO FULFILL ITS MISSION MEASURABLY THROUGH A BLEND OF SOUND MANAGEMENT, STRONG GOVERNANCE, AND A PERSISTENT REDEDICATION TO ASSESSING AND ACHIEVING RESULTS.

The literature regarding nonprofit capacity building is expanding as funders, infrastructure support organizations, researchers, and others interested in strengthening the sector work to develop a better understanding of how to build organizational capacity effectively. In the spirit of this inquiry, The Forbes Funds commissioned Judith Millesen, at the Voinovich Center for Leadership and Public Affairs at Ohio University, and Angela Bies, at the Bush School of Government & Public Service at Texas A&M University, to examine the incentives associated with engagement in capacity building. Specifically, the research team used organizational theory to frame an examination of the ways in which environmental characteristics, institutional attributes, and financial characteristics relate to the incentive to engage in capacity building.

The research presented in this report develops a comprehensive, empirical understanding of the incentive to engage in nonprofit capacity-building initiatives and addresses four key questions:

1. What are the primary incentives to (and, by extension, barriers to) nonprofit capacity building?
2. How do these incentives moderate (either facilitate or impede) engagement in nonprofit capacity building?
3. How do these incentives moderate processes of organizational change associated with nonprofit capacity building?
4. Do organizational attributes such as subfield focus, CEO tenure, or organizational age relate to issues of incentives?

THEORETICAL BACKGROUND

A common theme that runs through all three parts of a recent report on capacity building published by the Urban Institute (De Vita & Fleming, 2001) is how theory can be used to understand capacity building better. Specifically, the Urban Institute's Elizabeth Boris asserts "that the challenge faced by researchers is to sift through the growing body of experience on capacity building, link them to theory, and make this knowledge accessible and useful to practitioners and funders" (2001: 85). In direct response to calls for theory-based research, four mainstream organizational theories — **strategic management theory**, **resource dependence theory**, **agency theory**, and **institutional theory** — provide the framework for an analysis of capacity-building incentives. Four theories are used because, although each theory takes into account the critical relationship between the organization and its environment, each focuses on a different set of antecedent conditions to the actual capacity-building relationship, thereby painting an incomplete picture of a highly complex phenomenon.

Strategic management refers to the general process of "adapting the organization to its environment to better accomplish organizational purposes."[1] From a strategic management perspective, organizations make deliberate choices regarding mission, goals, resources, systems, and structures in order to better position themselves vis-à-vis the environment. The theory would predict that managers enthusiastically engage in capacity building to maximize resource use, structure the organization for optimal performance, and take advantage of external opportunities in ways that are responsive to constituent expectations.

Like strategic management theory, a **resource dependence** approach emphasizes the proactive role of the manager in shaping the organizational environment. However, unlike strategic management, resource dependence theory explicitly recognizes that there are likely to be power relationships that can restrict access to the resources necessary to implement meaningful change. Resource dependence theory would predict that nonprofit managers engage in capacity building in order to secure the resources needed for survival vis-à-vis their organizational competitors.

Agency theory uses the metaphor of a contract to describe the relationship between a principal, an agent, and a stake-holder. In a principal-agent relationship, principals delegate to agents the authority to act in a way that is consistent with the interests of the principal or the stakeholders. From an agency perspective, nonprofit managers are coerced into engaging in capacity-building activities so they can demonstrate their ability, worthiness, and success to those with accountability concerns.

The central premise of **institutional theory** is that organizations of the same type become increasingly isomorphic, or similar, to those in their environment over time. Institutional isomorphism occurs through coercive (dictatorial pressure to conform), mimetic (imitation as a response to uncertainty), or normative (stemming from professionalization) processes, each with their own set of antecedents. Table 1 summarizes the predictions each theory makes about why a nonprofit organization might engage in capacity building.

Methodology

A four-stage, multi-method research design was used to collect archival, qualitative, and quantitative data. Archival data included an environmental scan of the Pittsburgh capacity-building industry; review of promotional materials and web sites of local capacity-building providers and programs; and research into the funding priorities, grantmaking guidelines, and application procedures for seven of the major foundations in the region. Qualitative data was collected from 19 nonprofit executives who participated in one of five focus groups, and interviews were conducted with four foundation executives and 34 capacity-building professionals representing 31 different organizations. Quantitative data were collected from more than 200 Pittsburgh-area nonprofit organizations that responded to a web-based or mail survey.

Findings

In analyzing these data, it became apparent that no one theory could completely explain the incentive to engage in capacity building for two key reasons. First, theory-based analysis draws attention to the fact that some behavior can be interpreted using multiple theoretical perspectives. For example, while it certainly may be the case that nonprofit organizations engage in capacity building to satisfy contractual requirements, nonprofits may also seek technical assistance to improve programming and accomplish mission-related goals and objectives. Second, and more interestingly, the data collected for this study suggest incentives to engage in capacity building occur simultaneously and evolve over time. Two examples illustrate and describe this finding: simultaneous incentives and evolving incentives.

Simultaneous Incentives

Different theoretical perspectives can be used to interpret how nonprofit executives respond to complex expectations. Focusing on the theoretical interpretation of executive behavior has important implications for how to structure incentives, particularly because different rationales require distinct incentives to encourage capacity building. The challenge is to understand the motivating incentive so the interaction can be appropriately managed. The following quotation, from an executive director of a large human service organization, illustrates this point.

> *Now we have over a dozen projects that have people with them who we want to keep employed, and so from a programmatic perspective we need to keep reflecting on*

[1] Hodge, B. J. & Anthony, W. P. (1988). *Organization theory*. Boston, MA: Allyn and Bacon, Inc., 239.

TABLE 1. THEORY-BASED PREDICTIONS REGARDING THE INCENTIVE TO ENGAGE IN CAPACITY BUILDING

	STRATEGIC MANAGEMENT	RESOURCE DEPENDENCE	AGENCY THEORY	INSTITUTIONAL THEORY
Theoretical Premise	Organizations make deliberate choices about the external environment with regard to the organization's purpose, philosophy, and mission; key goals and objectives; allocation decisions; resources; and developing organizational structures and systems.	Organizations pursue various strategies to resist being controlled and constrained by other organizations, to mitigate dependent relationships, and to reduce environmental uncertainty.	Organizations respond as in a principal-agent relationship, where principals delegate to agents the authority to act in a way that is consistent with the interests of the principal or the stakeholders.	Organizations of the same type become increasingly isomorphic, or similar, to those in their environment over time. Institutional isomorphism occurs through coercive, mimetic, or normative processes.
Management Posture	Proactive	Proactive	Reactive	Reactive
Impetus to Engage	Internal forces	Internal forces	External forces	External forces
Basis for Engagement	Survival	Survival	Coercion	Normative reasons
Primary Purpose	Make better decisions	Secure resources	Appease funders	Seek legitimacy
Primary Use	Make strategic choices about internal operations and external opportunities	Create linkages; reduce environmental uncertainty; seek additional funding	Report to convey information to funders -OR- To conceal information from funders	Use is routinized -OR- Use is symbolic
Strengths	Holistic, proactive view of management operations	Highlights the need to align the organization and the environment	Promotes continuous goal assessment	Promotes legitimacy, reputation, and networking
Weaknesses	Overemphasizes rationalization and planning	Emphasizes only resource-based sources of power and control	Rooted in distrust	Compliance is often ritualistic, not purposive

> *what we do and ask ourselves does this still make sense? Are we doing what we are supposed to be doing?…Are we doing what the funders want to see?…You know there is board pressure. They have expectations as well…our clients also drive [some of our decision-making].*

Strategic management theory asserts that managers will willingly undertake capacity building so that they can improve decision making in ways that strengthen programs and in ways that are responsive to stakeholder expectations. From a strategic management perspective, this particular executive director is likely to respond to incentives that reward capacity-building efforts, especially given his reflection regarding organizational focus ("Does this make sense? Are we doing what we should be doing?").

Resource dependence theory focuses on the power relationships that restrict access to resources. The executive director in this example clearly recognizes there are resource dependencies to which he must attend ("Are we doing what the funder wants to see?"); this response, in turn, has important implications for the funding community and the structuring of incentives. Specifically, it is often assumed that organizations operating primarily from a resource dependence perspective are only building capacity because doing so provides income. Yet, as noted above, strategic management theory presumes organizations engage to enhance performance. *An important implication for the funding community is to structure incentives in ways that encourage strategic capacity building and discourage opportunistic engagement.*

The executive director also recognizes there are other stakeholders who have expectations for performance (e.g., the board and the clients), consistent with what institutional theory might predict. This means there may be an incentive to engage in capacity building that originates from these various stakeholders. In order to avoid tacit compliance to external expectations, there must be some type of accountability mechanism built into the process (consistent with what agency theory might predict). For example, when the board requires and sets aside funding for building organizational capacity, it must also insist upon some sort of evaluation report that demonstrates appreciable change in ways that are consistent with constituent expectations.

Evolving Incentives

Teasing out the "initial" and the "durable" incentive to engage proves to be especially difficult. What this means is not only are there multiple incentives to engage in capacity building that occur simultaneously, it is also that these incentives change or evolve over time. A story told by one of the capacity builders provides some insight. The capacity builder explained that an executive came to her because a funder required that executive to build management capacity. As the capacity builder made clear, the executive was very good at what she did (at least from a technical aspect), yet she was not a "great" manager.

If this were the only information the capacity builder had to go on, she might assume that the executive's motivations should be interpreted through an agency theory lens — the funder mandated compliance in an attempt to minimize agency costs associated with making a grant. From an agency perspective, the executive may have an individual motivation to engage in the training, or the executive may simply be complying with the mandate from the funder. The bottom line, however, at least from an agency perspective, is that unless required by the funder, there would have been no incentive to engage in the training. In this situation, it could be argued that the capacity builder's "client" is actually the funder, for it is the funder who is bearing the costs and benefiting from the interaction. This has profound implications for the interaction between the capacity builder and the nonprofit executive because the underlying assumption guiding the interaction presumes that neither is sufficiently motivated to "be in this for the long haul." From an agency perspective, both are interested in fulfilling the short-term expectations of their contracts, rather than embarking upon intensive efforts to build long-term, sustainable capacity.

When the capacity builder interviewed the executive prior to undertaking the management training (as requested by the funder), the capacity builder learned more about the executive's motivations. The executive did acknowledge that the initial incentive to engage was to comply with the funder's request, yet she also noted that in talking with colleagues and peers, it became apparent that capacity building could be leveraged to secure future financial contributions. This suggests that although the initial incentive was to comply with an external mandate, the information received from peers further advanced the executive's desire to copy practices others had found to be successful. This example provides two different theory-based interpretations of the incentive to engage, each with very different implications.

Institutional theory predicts that organizations will ritualistically undertake specific activities in an effort to be deemed legitimate by those external to the organization. The executive admitted she was hoping to leverage the training so that she could acquire additional funding. It could be argued that engaging in the training would provide the executive with the legitimacy needed to appease a demanding funding community that recognizes and rewards capacity building. The problem is that when the primary incentive is to gain legitimacy, conforming to external expectations (i.e., mimicking the successful behavior of others) is not likely to result in substantive changes in behavior or organizational operations. Thus, from an institutional theory perspective, the interaction between the parties and the implications are similar to what agency theory might predict.

Alternatively, resource dependence theory predicts nonprofit managers will proactively seek capacity building initiatives to promote organizational performance so they can secure the resources needed for survival. Implicit in the resource dependence perspective is that the organization is hoping to alter the power dynamics that restrict access to resources. This means that savvy managers will want to demonstrate any appreciable change resulting from their participation in capacity-building initiatives. Moreover, given that estimations of organizational effectiveness and legitimacy are externally conferred (often by those in power or those providing the resources), these changes are likely to be consistent with mission-related goals and objectives.

The deterministic frameworks of both agency and institutional theory provide some insight as to why many nonprofit executives complain about "one-size-fits-all" approaches to capacity building (Millesen & Bies, 2004). Capacity builders who believe that clients engage in the capacity-building initiatives only to satisfy the expectations of those external to the organization might shy away from developing unique, context-specific programs tailored to meet the individual needs of a specific organization. If, however, the capacity builder were to interpret the legitimacy-seeking behavior using the underlying assumptions of resource dependence theory or even strategic management theory, the outcomes (both in the training agenda and in management behavior as a result of the training) might be different. Both perspectives arguably predict managers will aggressively seek ways to improve chances of survival in an increasingly complex and competitive environment. As such, resource dependence theory would predict that managers are more likely to embrace practices that give them a competitive edge.

Thinking of incentives as simultaneous influences or evolving processes may be what is needed to institutionalize a "culture of continuous improvement," particularly because, as these data suggest, initial incentives are likely to be very different from the enduring motivation to engage in ongoing continual improvement. What starts as a response to an agency-related mandate or a reaction to resource dependencies can ultimately evolve into a strategic management orientation that becomes institutionalized over time.

Understanding the incentive to engage in capacity building is unexpectedly complex, having elements that reflect the underlying theories of all four theoretical perspectives used to inform this study. The four theories present distinct views about how organizations operate and, as such, each provides different insight and suggests different strategies for the primary stakeholders in a capacity-building relationship. Some information is more practical for funders, some more useful for organizations, and still some more helpful for practitioners. Consequently, structuring incentives in ways that embrace the assumptions of these theories is going to be largely dependent upon on what an organization, or a funder, is hoping to achieve.

Implications

The theory-driven research presented here highlights the complex and dynamic nature of the incentives related to engaging in nonprofit capacity building. The findings suggest it is critical to structure incentives in ways that integrate the assumptions of more than one theory. Possibilities include:

- Encourage incentives to build capacity throughout the organization;
- Develop "soft" incentives that promote mutual benefit;
- Promote incentives that recognize managerial complexity;
- Offer incentives that discourage competition and promote collaboration;
- Create incentives that integrate the assumptions of multiple theoretical perspectives and evolve over time; and
- Establish incentives that recognize and build upon the foundation community's predisposition to provide programmatic support.

READ THE COMPLEMENTARY ANALYSIS TO THIS STUDY: 2005 TROPMAN REPORT VOLUME 4, NUMBER 3 — *Nonprofit "Capacity-Building Orientation": The Role of Learning in Building Nonprofit Performance*. ALSO, FOR MORE INFORMATION ABOUT THE CRITICAL MATTERS FACING NONPROFIT TRUSTEES AND STAFF AND THE RESULTING NEED FOR CAPACITY BUILDING, POINT YOUR BROWSER TO WWW.FORBESFUNDS.ORG AND DOWNLOAD A COPY OF *Facing the Futures: Building Robust Nonprofits in the Pittsburgh Region*, BY DR. PAUL C. LIGHT, NEW YORK UNIVERSITY AND THE BROOKINGS INSTITUTION.

TO READ THE FULL TEXT OF THIS STUDY, LOG ONTO THE FORBES FUNDS WEBSITE AT WWW.FORBESFUNDS.ORG.